FILE COPY

FILED
APR 17 1950
CHARLES ELMORE CROP

No. [redacted]763

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1949

DEBOTHEZAT IMPELLER COMPANY, INC.,
Petitioner,

v.

AMERICAN MACHINE AND METALS, INC.,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

McLAUGHLIN, STICKLES & HAYDEN,
Attorneys for Petitioner.

SAMUEL WILLISTON,
CHESTER B. McLAUGHLIN,
WATSON WASHBURN,
Of Counsel.

INDEX

	PAGE
PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT	1
OPINIONS BELOW	1
JURISDICTION	2
QUESTIONS PRESENTED	2
STATEMENT OF CASE	2
SPECIFICATION OF ERRORS TO BE URGED	6
POINT I—The decision below conflicts with New York law in not considering extraneous evidence to explain the meaning of an ambiguous contract	6
POINT II—The decision below conflicts with the law of New York State under which it would be unreasonable and inequitable to permit Metals in form to terminate its contract and then to continue in the same business without further payments	15
POINT III—The striking of the four equitable defenses was contrary to New York Law	20
CONCLUSION	26

TABLE OF CASES

PAGE

Cammack v. *Slattery & Bros., Inc.*, 241 N. Y. 39, 148 N. E. 781 (1925) 8, 15, 17, 18, 19

Clark v. *Carolina etc. Ry. Co.*, 225 N. Y. 589, 593.... 10

Conmar Products Corp. v. *Universal Slide Fastener Co., Inc.*, 172 F. 2d. 150, 156 13

Eskimo Pie Corp. v. *National Ice Cream Co.* (C. A. 6) 26 F. 2d 901, 902 19

Friedman v. *Connecticut General Life Ins. Co.*, 251 A. D. 292 23

Fleischman v. *Furgueson*, 223 N. Y. 235, 241..... 10

Lipman v. *Niagara Fire Ins. Co.*, 121 N. Y. 454, 460.. 23

May v. *Hettrick Bros.*, 181 A. D. 3 ..... 23, 24

Meinhard v. *Salmon*, 249 N. Y. 458 25

New York Tel. Co. v. *Jamestown Tel. Corp.*, 282 N. Y. 365, 26 N. E. (2d) 295 (1940) 16, 17

Russell H. & I. M. Co. v. *Utica D. F. & T. Co.*, 195 N. Y. 54, 87 N. E. 788 ..... 24, 25

Selwin & Co. v. *Waller*, 212 N. Y. 507, 106 N. E. 321.. 23

Von Bremen v. *McMonnies*, 200 N. Y. 41..... 14

STATUTES

FEDERAL:

Judicial Code J. C. as Amended by the Act of February 13, 1925:
Section 240A 2

25 Am. Bar Ass'n Jour. 855, 28 U. S. C. A. 500 (Oct., 1939), 856 20

1 Moore, Federal Practice, page 817 20

IN THE

Supreme Court of the United States

OCTOBER TERM, 1949

No. 102

DEBOTHEZAT IMPELLER COMPANY, INC.,
Petitioner,
v.
AMERICAN MACHINE AND METALS, INC.,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioner prays that a writ of certiorari issue to review the judgment of the Court of Appeals for the Second Circuit entered in this case.

Opinions Below

The opinion of the District Court dismissing Petitioner's four equitable defenses before trial (208-239*) is reported at 82 F. Supp. 556.

The District Court rendered no written opinion after the trial, but the oral statements of the District Judge in deciding the case are set forth at pp. 381-418. The opinion of the Court of Appeals (pp. 628-45) is not yet reported officially, but appears in C. A. (2d) Docket #21487, decided January 17, 1950.

---

* All undesignated references are to pages of the Record.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered on January 17, 1950 (p. 646). The jurisdiction of this Court is invoked under § 240A of the Judicial Code J. C. as amended by the Act of February 13, 1925.

Questions Presented

I. Whether the written contract was ambiguous under New York law.

II. Whether one who has agreed to purchase a business including know-how, fundamental aerodynamical principles, formulae, experimental data, unique designs, customers, etc., upon cancelling the purchase agreement may continue to carry on the business and use all such material without further payments.

III. Whether assuming such rights of cancellation and continuance of the business would otherwise exist, they can be exercised without any restriction where the purchaser's inequitable conduct in violation of its contractual obligations would prevent the seller from resuming its business as agreed, thus causing the seller irreparable injury.

Statement of Case

The background of this litigation is succinctly stated in the opinion of the Court of Appeals as follows (with certain indicated additions):

"The appellant, DeBothezat Impeller Company, Inc.," (hereinafter called DeBothezat) "is a Delaware corporation which then was, and for some years previously had been, maufacturing and selling impeller blowers and related products for the movement of air in accordance with

the principles advocated by Mr. DeBothezat, a skilled engineer in this field. It was in part protected by United States patents covering his inventions. The business had not, however, been a financial success" (though its gross sales already exceeded $725,000, p. 174) "and arrangements were made for the appellee" (hereinafter called Metals, a large holding company which operated a number of different businesses, none of them in the ventilating field) "to take it over together with the plant, equipment, patents and all other assets of the appellant including unfinished products being manufactured, and conduct it at its own expense. Appellee was to pay the appellant certain stated percentages of the annual aggregate net sales, with a minimum monthly payment which was to be credited against the over-all amount as and when more became due. After a fifteen year period of operation, however, the appellee had the option to give a notice of three months that it elected to pay a sum, equaling the aggregate of all payments which had become due under the contract during the preceding six years, in full discharge of its liability to pay thereunder." [The above payments were to be "in no way diminished by reason of the expiration or invalidation of any Letters Patent granted hereunder or the rejection of any application therefor." (18).]

"There were provisions, written with careful attention to detail, to the effect that there should be transferred to the appellee all of the appellant's patents and patent applications and its plant, records, inventory and all of its equipment except some which was leased to the appellee. Appellee was given the right, however, to use and dispose of the plant equipment as it pleased and at the end of a stated period" (for six months) "to purchase the leased equipment at the nominal price of one dollar. Additional provisions required the appellee to feature the name 'DeBothezat' in the sale of the products made under the contract; 'to use its best efforts' to promote sales; and to furnish adequate audits of its operations.

"The contract ran for an indefinite time, but appellee was given the right to terminate it at any time after the expiration of one year by giving the appellant six months' notice of its election to do so and in the event of such termination appellee was required to transfer to the appellant all the patents it had obtained under the contract and also any other patents or patent applications it had for the contract products, providing the appellant reimbursed it for expenditures it had made in connection with their issuance or prosecution respectively. And for one year after such termination of the contract the appellant was given an exclusive license under them regardless of reimbursement. The appellee was also bound to convey and deliver to the appellant all of the plant and equipment, which it had on hand, that it had received from the appellant under the contract and to permit the appellant to inspect its books and records relating to the contract business and to make copies of them.

"The appellee took over the appellant's business and property connected therewith and has since been operating under the contract, which had been modified by mutual consent at times in ways not now material. It was contemplated when the contract was executed that the appellee would form a new corporation, having the name 'DeBothezat' in its title, to which the appellee would assign the contract and which would carry it out. This was done and for a while the new corporation did conduct the business pursuant to the contract but later that corporation was dissolved and merged into the appellee which has since conducted the business in a successful manner.

"In 1946, when the most valuable DeBothezat patent was about to expire" [actually, the basic patent did not expire till August 19, 1947 (146-151)], "the appellee took up with the appellant the question of its right to terminate the contract and then continue to make products the same as, or similar to, the contract products. The discussion which followed brought to the surface differences between the parties

as to the meaning of certain provisions in the contract relating to this subject and such attempts as were made to reconcile these differences failed.

"Metals then brought this action for a declaratory judgment that it could terminate the contract and continue the business exactly as before, provided it infringed no DeBothezat patents.

"DeBothezat contested this claim, and further interposed six equitable defenses and counterclaims: one of these was to reform the contract to prevent Metals' proposed action, if the contract as drawn were held to permit it; and four others which alleged that Metals had converted or destroyed the leased equipment, refused to furnish reasonably detailed audits, suppressed the DeBothezat name in conducting the business, and failed to use its best efforts to promote the business."

The District Court after a pre-trial conference dismissed the four equitable defenses (pp. 70-80; 82 F. Supp. 556), holding that even if Metals were a joint adventurer, and its misconduct had so impaired the good-will and facilities of DeBothezat as actually to prevent DeBothezat from resuming its fan business, enabling Metals to appropriate the whole business to its own use, and causing DeBothezat irreparable injury, nevertheless under the law of New York State the court had no power to stay Metals' exercise of an otherwise existing right to cancel and continue to carry on the fan business. Having dismissed the four defenses, it severed the four counterclaims alleging the same facts, and directed that they be separately tried later. The Court of Appeals affirmed. This holding is the subject of Point III, *infra*.

At the trial the District Court held there was no evidence to justify reformation; that the written contract unambiguously gave Metals the right to cancel and carry on the fan business; and that consequently no evidence outside the contract showing a contrary intention (of which there was

abundance) could be considered. The Court of Appeals' affirmance of this holding is the subject of Points I and II, *infra*.

Specification of Errors to be Urged

The Circuit Court of Appeals erred:

1. In holding that the written contract under the New York law unambiguously permitted Metals to continue in the fan business after cancelling the purchase agreement.

2. In holding that under New York law Metals could continue to use all the intangible assets which it acquired under the purchase agreement without further payments therefor, after cancelling the agreement.

3. In holding that under New York law, assuming such rights of cancellation and continuance of the business would otherwise exist, they can be exercised without any restriction where the purchaser's inequitable conduct in violation of its contractual obligations would prevent the seller from resuming its business as agreed, thus causing the seller irreparable injury.

POINT I

The decision below conflicts with New York law in not considering extraneous evidence to explain the meaning of an ambiguous contract.

1. In essence, Metals, a large holding company, managing many lines of business (none in the ventilating field), bought the DeBothezat fan business on the installment plan, with an option to accelerate payment and also the alternative option to cancel the purchase contract. The decisions below have held that Metals can cancel the purchase contract and continue the same fan business under its own name (which the Court of Appeals considered more like a

lease than a purchase, footnote 4, p. 639), without paying the remainder of the purchase price. They hold that the contract on its face unambiguously gives Metals this right, and so have refused to consider the abundant evidence in the record, from the beginning of the negotiation through the various drafts of the agreement to its final signature, and for twelve years thereafter, which proves beyond doubt that the parties intended that Metals could not keep the business without paying for it.

The contract naturally must be interpreted not from hindsight, but as it looked to the parties in 1934. DeBothezat was surrendering everything to Metals, not only its patents and all its equipment, but its customers' lists, plans, specifications and general know-how of the ventilating business. Its name, its patents, and its machinery it could get back in case of cancellation, but not the knowledge of its business and the impediment caused by the interruption of its operations for at least a year and a half. Under the terms of the contract (p. 16) Metals was obligated to pay to DeBothezat as a minimum only the sum of $413.33 a month (that is $5,000 a year), beginning one year after the date of the contract. By the same token (p. 18), at the end of one year Metals could have given notice of cancellation effective six months thereafter, so that all it was obligated to pay, both for having obtained a complete grasp of DeBothezat's specialized knowledge and experience in the fan business and for having caused DeBothezat to cease operations (p. 23) was $2,500.

Thus, if Metals' interpretation is correct, it could have virtually put DeBothezat out of business, learned how to operate the fan business itself, and then entered into competition with its unfortunate and almost helpless victim on the most favorable terms for a mere $2,500 payment. It seems inconceivable that DeBothezat would have been so foolish as to have given away its business (representing a cash investment of $180,000., p. 174), on such terms. Incidentally, however, it may be noted that if DeBothezat

did put itself in Metals' power to such an extent, it greatly emphasizes the quasi-fiduciary duties of Metals, which are discussed in Point III, *infra.*

One would suppose that only the clearest language could justify any Court in such an unusual and apparently unfair construction of a purchase contract, in the teeth of all the evidence outside the contract leading to a more reasonable interpretation. This is particularly true under New York law, which has held in a closely analogous case that "it would be unreasonable and inequitable to hold that the defendant might in form terminate its contract and then continue to manufacture radiators without the payment of any royalties such as it had agreed to pay." *Cammack* v. *Slattery & Bros., Inc.,* 241 N. Y. 39. See Point II, *infra.*

Amazingly enough, when the contract is examined, we find that there is *not one word in it which expressly permits Metals to continue the fan business after cancellation.* The only words on the subject (we claim) expressly negative any such right, but at the very least are ambiguous enough to let in explanatory proof.

These words are found in Paragraph THIRTEENTH of the contract, as follows:

> "THIRTEENTH: The DeBothezat Company hereby consents to the use of the name 'De Bothezat' in the corporate title of the New Company and to the sale of the Products thereof under the name 'DeBothezat.' Metals Corporation agrees that it will use the name 'De Bothezat' in its literature and sales promotion in connection therewith. Upon the termination of this agreement, the right of Metals Corporation or the assignee of its interest herein to use the name 'De Bothezat' for any purpose shall cease. Metals Corporation further agrees that the New Company will not engage in the manufacture and sale of any products which compete with the Products to be manufactured and sold hereunder."

DeBothezat claims that the last sentence applies (like the preceding one) "upon the termination of this agreement." Metals claims it applies only during the life of the agreement.

Obviously if the last two sentences were connected by a semi-colon instead of a period, Metals would have no right to continue this fan business after it terminates the contract. It would seem that a question which depends upon such a subtle nuance of punctuation would *per se* be ambiguous enough to make extraneous evidence of intent admissible. DeBothezat's interpretation seems further supported by the use of the words "further agrees" which appears to tie the two sentences together. The Court of Appeals at p. 634 of its opinion states that this argument "as will appear," is fine-spun, but it then proceeds to meet the argument "on its own plane"—conceding that its own counter-argument is fine-spun, as it certainly seems to be. But then the Court, saying that "we of course put no reliance on the parallel," states that the first three sentences of Paragraph THIRTEENTH above quoted are to be read together while the fourth sentence is unrelated to them. The only reason it gives for this interpretation, instead of reading the third and fourth sentences together, is that the agreement not to compete in the fourth sentence is limited to "the products to be manufactured and sold hereunder," thus, it infers, limiting the duration of the non-competitive agreement to the life of the contract, since thereafter no products could be sold and manufactured "under the contract." Here again the Court necessarily encounters another ambiguity, and it concedes that DeBothezat "rather ingeniously asserts that the words 'products to be manufactured and sold hereunder' mean simply the type or kind of products manufactured" during the contract. That DeBothezat's explanation is not only ingenious, but also correct, seems more likely from the fact that DeBothezat's own agreement not to compete which follows immediately

in Paragraph FOURTEENTH, applies expressly "during the life of this agreement" only.

Without pursuing further the rather tenuous arguments of the Court of Appeals, it seems clear that the net result (as the Court says of the position of the "non-competitive" sentence) "is wholly inconclusive." In such a situation, New York law requires that outside evidence be received to explain ambiguous language, particularly to avoid a construction which will give one party an unfair advantage over the other, *Fleischman* v. *Furgueson*, 223 N. Y. 235, 241, or to conform to their long-continued conduct. *Clark* v. *Carolina etc. Ry. Co.*, 225 N. Y. 589, 593.

DeBothezat's most vital evidence outside of the contract itself proving that the parties intended that Metals should not, if it cancelled, compete thereafter with DeBothezat, may be briefly summarized as follows:

1. An intercompany memorandum (pp. 467-8) from Metals' chief executive (then as now P. G. Mumford) to its executive vice-president, Holder, dated November 21, 1933, outlining the whole proposal, and in particular the three alternatives which Metals would have as to permanent continuation of the business or going out of it, says:

> "6. After the first year, we have an option to cancel this contract on six months notice, and to return the machinery taken over in good condition, less ordinary wear and tear.
>
> "7. 15-year option at six times average annual payments last five years.
>
> "8. If option not exercised we may continue indefinitely at one-half the former royalties without guarantee."

The "option" referred to in "8" is obviously that outlined in the preceding paragraph "7". Had Mumford intended to refer also to the option contained in paragraph "6" he would have used the plural instead of the singular.

Thus we find the same three choices which appear in all the drafts and in the final contract, that is, to cancel and go out of the fan business, to terminate payments after fifteen years with a commutation payment equal to six times average annual payments for the last five years, or a right to "continue indefinitely" at one-half rates if the commutation option is not exercised.

It was so clearly implied in "6" that it was unnecessary to spell it out, that if the option to cancel were exercised, Metals would have to stop selling fans, for otherwise the options offered by "6" and "8" would be to cancel the contract and continue the business without payment or to continue the business paying one-half of the former payments—in other words, an option to pay or not to pay for the same thing.

This memorandum of Mumford's also disposes of the point made in the opinion below that the purchase option involved a different set of circumstances and results from the cancellation option. Clearly, Mumford had in mind either the continuation or cessation of the business. The return of the DeBothezat name, patents, etc. were merely details subsequently worked out by the lawyers to effectuate the purpose of Mumford's memorandum.

2. In a memorandum from Holder to Mumford less than a year after the contract went into effect (pp. 590-1) Holder disclosed his understanding that payments had to be paid on all products, regardless of whether or not covered by the DeBothezat patents, and he said that if Metals did not want to do this, it would either have to negotiate a new contract with DeBothezat or go out of the fan business (p. 591).

This memorandum was given to Washburn by Holder and Mumford as representing Metals' views (p. 204).

3. No suggestion was ever made by Metals until February 18, 1946 (p. 159) that it could cancel the contract and still continue in the fan business even though it had been

making repeated efforts during the intervening twelve years (pp. 211-7, 472, 565-7, 592) to buy out DeBothezat at a bargain and was doing everything to beat down the price, including the drastic step of giving notice of cancellation, later withdrawn (p. 471).

4. As showing Metals' uncertainty as to the meaning of the contract, it is also significant that no notice of termination was given after the expiration in 1946 of what Metals describes as the last patent which it was using (pp. 432, 454).

5. Washburn's testimony (confirmed by Holder and not denied by Mumford) that just before the contract was signed, Mumford and Holder agreed with him that Metals must go out of the fan business if it cancelled, while apparently considered by Judge Coxe not sufficient to show a mistake justifying reformation, is strong evidence in interpreting any ambiguity.

6. Holder testified as to Metals' obligation to go out of the fan business if it cancelled (pp. 248-9):

> "There was also a question that if we decided to get out of the fan business, could we continue or not our main business, and the so-called escape clause that I mentioned before was that we wanted to feel that we could dip our toes in the water; if it felt too cold, we wouldn't swim; and if it felt right, we could swim, and that is exactly the position we took; if we wanted to stay in the fan business we would stay with DeBothezat, and if we didn't want to stay in the fan business we would get out of it."
>
> • • • •

(p. 309)

> "Q. Did you ever say to him [Washburn] during this period of negotiation that you were unwilling to agree not to continue in the fan business if you cancelled? A. No, it was my understanding that we would not continue in the fan business if it was cancelled.
>
> Q. Did you convey that idea to the other side? A. Yes."

We submit that the above proof would not only have supported a finding by the Trial Court in DeBothezat's favor, but that its cumulative effect would have almost compelled such a finding.

The Court of Appeals itself referred to outside evidence as its final argument (p. 641), this being the fact that there were seven drafts "before agreement was finally reached." Surely this has no bearing on the question of the ambiguity of the final agreement, and the court does not so assert. It uses this evidence as the basis for a conclusion that DeBothezat's attorneys were to blame for the ambiguity. Where one party has superior knowledge or skill that party may be chargeable with an ambiguity, but here both parties were represented by competent lawyers. Metals' attorneys should have been quite as careful to express clearly Metals' right to continue the purchased fan business without paying for it, under certain conditions, as DeBothezat's to express clearly the opposite intention.

What makes the Court's reliance on the seven drafts particularly unfair is that the wording of these successive drafts, as explained in the testimony, was an important element in proving that the parties intended precisely what DeBothezat now claims (pp. 192-202, 237-8).

Actually, one may infer from the opinion that the Court was influenced in its interpretation of this contract by its peculiar theory that individual wrong-doers should never be prevented from competing, wherever the innocent general public has that right. The opinion (p. 648) refers in support of this position to *Conmar Products Corp.* v. *Universal Slide Fastener Co., Inc.*, 172 F. 2d. 150, 156, which concedes (at p. 155) that this doctrine is peculiar to the Second Circuit and is in conflict with the Sixth and probably the Seventh Circuits, which hold that in patent cases "if before issue one has unlawfully obtained and used information which the specifications later disclose, he will not be free to continue to do so after issue; his wrong deprives him of

the right which he would otherwise have had as a member of the public." Whatever may be the correct rule as to patent cases (which this is not), there seems to be no doubt that the public interest would be best served in our case by having one DeBothezat fan business carried on, whether by DeBothezat or Metals, rather than having the business divided between two companies, both using Chinese copies of the other's products.

Further to bolster its construction, the Court of Appeals asserts (p. 642) that "the agreement not to compete" *might* be illegal, because "it would not be ancillary to the sale of, or reversion of a sold, business." But this seems to be arguing in a circle, for if DeBothezat is correct, the business would revert to it. The Court states (foot-note 4) that Metals "retains after termination its own factory, equipment, raw material, trade-marks, good-will, distribution facilities and the like" in support of its holding "that the contract here is more like a lease than a sale of a business." In the first place, whether it was a lease or a sale seems immaterial. And again, this seems to be a circular argument, for if DeBothezat is right, Metals would not retain the trade-marks, good-will, distribution facilities, or anything else relating to the fan business. Metals carries on a number of other businesses, with factory, good-will, trade-marks and distribution facilities which it of course retains. As to the fan equipment and raw materials, there is uncontradicted testimony that the reason why Metals would not agree to turn over its fan machinery and files bodily and gratis to DeBothezat was that it could use these in its other businesses, or sell the machinery second-hand (pp. 197, 198).

If the Court of Appeals meant that after turning back the fan business to DeBothezat, Metals could continue to use the trade-marks and good-will of that business, or sell to its customers, its holding would be again contrary to New York law, assuming a joint venture relationship between the parties is established (see opinion below at pp. 647, 648) *Von Bremen* v. *McMonnies*, 200 N. Y. 41.

That there is no question of the legality of the non-competitive clause seems clear from Restatement, Contracts, § 516:

> "(b) If a sale of the business is made to one who previously was not a competitor, it is obvious that there is no diminution of competition by the sale and the promise accompanying * * * Nor is the promise invalidated by the circumstance that nothing tangible is transferred so that the transaction amounts merely to the sale of good-will accompanied by a promise not to engage further in a competing occupation."

The Court's preoccupation with patent law and supposed unlawful restraint of competition permeates its whole opinion, and while it concedes that "here something more than a license agreement is involved" (p. 639), significantly the only holdings upon which it relies are patent cases. In reality, this case has nothing to do with patents or monopolies. It is purely a case where Metals is trying (with success, so far) to evade the final payment of approximately $175,000 for the purchase of the DeBothezat fan business. As P. G. Mumford blurted out unresponsively when called to the stand (345): "We think he" (DeBothezat) "is making enough money off us."

POINT II

The decision below conflicts with the law of New York State under which it would be unreasonable and inequitable to permit Metals in form to terminate its contract and then to continue in the same business without further payments.

The New York Court of Appeals in *Cammack* v. *Slattery & Bro., Inc.*, 241 N. Y. 39, 148 N. E. 781 (1925), held that such a construction of a contract would be "unreasonable" and "inequitable."

There the parties entered into a contract which provided for the manufacture by defendant of radiators which em-

bodied ideas and conformed to plans developed by the plaintiff. The defendant agreed to pay the plaintiff certain royalties on radiators thus manufactured and sold by it. There were no patents involved. The contract contained no termination date. Some six years after it had been entered into, the defendant gave written notice of termination, but nevertheless continued to manufacture in accordance with plaintiff's ideas and plans. The Court held unanimously (as had the lower courts) that, inasmuch as no expiration date was fixed by the contract, the defendant had the right to terminate at any time, but that its notice of cancellation was ineffectual because it continued to manufacture and sell the radiators and therefore did not, in fact, terminate the contract.

Hiscock, Ch. J., said (p. 45):

> "Under these circumstances this argument of defendant becomes quite academic because, of course, it would be unreasonable and inequitable to hold that the defendant might in form terminate its contract and then continue to manufacture radiators without the payment of any royalties such as it had agreed to pay."

The *Cammack* case has since been cited with approval by the New York Court of Appeals in *New York Tel. Co.* v. *Jamestown Tel. Corp.*, 282 N. Y. 365, 26 N. E. (2d) 295 (1940).

There, after the expiration of a contract, the parties continued to do business together. There was no dispute as to the liability of the defendant to make payment, for, as Lehman, Ch. J., said (p. 371):

> "Obligation to pay for benefits received is not denied by the defendant. The issue between the parties is whether the amount to be paid must be measured in accordance with the terms of the express contract or in accordance with an implied contract to pay the reasonable value of such benefits."

The case differs from the present case in that there each party continued (and, being public utilities, had to continue) performance after the expiration of the contract, while here the consideration moving from DeBothezat was substantially all given when the contract was entered into, and accordingly, on termination, Metals will have received everything for which it promised payment.

Lehman, Ch. J., in *New York Tel. Co.* v. *Jamestown Tel. Corp., supra,* distinguished the *Cammack* case on this ground. He said (pp. 373-4):

> "The obligation of a contract terminable at will to pay royalties for the right to manufacture an article, according to plans and designs of another person, continues until the contract is effectually terminated, and effective termination does not arise from mere notice of intention without relinquishment of benefits derived from the contract. In such case notice of intention is completely negatived by acts. Notice of intention to terminate a contract is an empty gesture where it appears that the intention is to terminate only the obligation imposed by the contract and not the right to benefits derived from the contract, for the contract gives no right of partial revocation."

Thus, the gross unreasonableness, or even the impossibility of a supposed alternative to pay or not to pay for what has been received is firmly established by the highest Court of the State of New York.

When the *Cammack* case was called to the attention of the trial judge, he admitted frankly, after reading it, that he did not "understand that case too well" (p. 404), and his subsequent statements seem to bear this out, as he could not seem to get doctrines peculiar to patent law out of his mind (pp. 405-8).

The Circuit Court of Appeals attempted to distinguish the *Cammack* case on the ground that because several *express* conditions applied on termination of the contract

here, no other condition would be implied, and also that Metals was expressly required to give back the original patents (all expired!) and any fan patents of its own (none being now essential (p. 616)).

The distinction seems unreal. For none of the express conditions are inconsistent with the implied *Cammack* covenant, but on the contrary are all aimed at facilitating the resumption of the fan business by DeBothezat, which is entirely consistent with its abandonment by Metals. It is ridiculous to suppose, for example, that if the *Cammack* agreement had expressly provided for termination at will by the grantee, or had further provided that if the grantee terminated, he should assign any patents he might have obtained on the radiators to the grantor, and should also supply a list of his customers, this would have changed the court's opinion that it was both *unreasonable* and *inequitable* to permit the grantee to continue making plaintiff's radiators without paying for them.

The New York law, as authoritatively laid down in *Cammack,* sees not even a hint of illegality in requiring the defendant to pay for what it uses, or else to give it up; it is not concerned whether Cammack's radiator arrangement was a lease or a sale, or with the fact (also referred to in the opinion below in footnote 4, p. 639) that the defendant "retains after termination its own factory, equipment, raw materials, trade marks, good will, distribution facilities and the like,"—of course, the *Cammack* rule would preclude retention of any trade marks or good will of the "contract business."

The opinion below seems wholly in conflict with New York Law in applying to this contract for the sale of a business, including principles, formulae and designs both patented and unpatented, a narrow rule of construction which requires that a restriction preventing former patentees from attacking a patent "be in such express and clear words that the intent could not be doubtful,"—quoted at

p. 639 from *Eskimo Pie Corp.* v. *National Ice Cream Co.* (C. A. 6) 26 F. 2d 901, 902, which the court thought "closely apposite." On the contrary, the New York law appears to be exactly the reverse, as applied to the sale of unpatented designs,—they cannot be used without compensation unless the agreement expressly provides otherwise.

The opinion below also errs in the opposite sense in its analysis of the *Cammack* decision. The latter does not "imply the condition upon termination of going out of the radiator business", but only of stopping the manufacture and sale of *the type of radiator it acquired from the plaintiff*. As applied here, the New York law evidently requires that even if DeBothezat had transferred to Metals merely unpatented and unpatentable designs of fans, instead of a business in which $180,000 in cash had been invested, and even if there were no provision whatever preventing Metals from competing with the DeBothezat fans, either during or after the contract, the New York courts would consider it "unreasonable and inequitable to hold that the defendant might in form terminate its contract and then continue to manufacture radiators without the payment of any royalties such as it had agreed to pay". It necessarily follows that if the manufacturer terminated its contract, it could continue in the radiator (or fan) business only with the limitation, not that it must refrain from *infringing upon valid patents owned by its grantor after such termination* [the meaningless language (p. 620) in the decree affirmed below, suggested in Metals' prayer for relief (p. 7) which applies equally as well to the public at large as to Metals] but that *it must refrain from using any designs, mathematical principles, theories or ideas, patented or otherwise, derived by it from DeBothezat.*

POINT III

The striking of the four equitable defenses was contrary to New York Law.

After Judge Ryan had held on August 12, 1949 (8 F. R. D. 306) that the validity of the four separate equitable defenses presented a serious legal issue which could not be determined on a motion to strike, it seems unusual that at a pre-trial conference held shortly thereafter, the same defenses should have been stricken without the appellant having had any opportunity whatever to examine the appellee before trial.

As stated in 1 Moore, Federal Practice, page 817:

> "While Rule 12 does to some extent provide for speedy disposition of certain matters preliminary to trial, it does not seem to have been contemplated that the court should ordinarily supplement Rule 12 by proceedings under Rule 16, which is quite apparently designated for use at a later stage in the litigation."

The same principle was more specifically stated by Judge Laws in 25 Am. Bar Ass'n Jour. 855, 28 U. S. C. A. 500 (Oct., 1939), at page 856.

> "It becomes obvious from what has been said that it is essential that a case should be substantially prepared for final trial prior to the time it is heard at pre-trial. This point cannot be too strongly stressed."

Judge Knox stated at the pre-trial conferences that in order to justify dismissal of the four equitable defenses, he must assume that the defendant could prove all facts and circumstances in any way relevant to these defenses. Accordingly, appellant submitted two memoranda outlining the scope of possible proof, much of which would have to be obtained from the pre-trial examination of the appellee.

Whether or not the 1934 contract permitted Metals to continue in the fan business after cancellation, there is no

doubt that DeBothezat was meant to have the right to resume that business. The four *equitable defenses* are based on the alternative that Metals would have the right to cancel and continue the fan business but for its unfair conduct directed toward impairing the ability of DeBothezat to resume the business in competition with Metals.

That the acts charged in these defenses would impair and might even destroy DeBothezat's capacity to resume operations, and thus cause irreparable injury, seems beyond question, and is conceded in the opinion below.

DeBothezat entrusted its property and going business to Metals, under a contract requiring it to use its best efforts to build up both the business and the DeBothezat name, to make reasonably detailed reports of its sales (which would enable DeBothezat to follow the trend of the business and make plans for the future accordingly), and to return the leased machinery in the event of cancellation.

DeBothezat informed Judge Knox that it expected to prove: (1) the destruction of the leased equipment; (2) the refusal of Metals to furnish the required information as to the sales of the various subdivisions of the business, so that DeBothezat could not plan in advance its campaign to reestablish its business along the most profitable lines, as contemplated by the contract; (3) Metals has gradually minimized the DeBothezat name, and finally, as to the largest single division of the business, suppressed it entirely, taking out a trade-mark for this division under the name "Fan-Pac," which Metals has extensively advertised, hoping to continue this largest division of the business for its own benefit on cancellation without the slightest interruption, and to exclude DeBothezat from its benefits; (4) instead of using its best efforts to promote DeBothezat sales, Metals has devoted a large part of the time and attention of its fan personnel to devising means of most effectively appropriating the entire fan business to its own benefit, and of preventing DeBothezat from re-entering the business.

It seems clear that the misuse of the "Fan-Pac" division alone might make the difference between the profitable resumption of the business by DeBothezat and bankruptcy. The combination of all the violations of duty would have a cumulative effect.

The injury to DeBothezat through loss of the chance of regaining its business (now selling over a million dollars a year) would be plainly irreparable, for it could not properly be compensated by damages, the amount of which would be speculative and difficult to prove.

The crux of the opinion below is its acceptance of the District Court's conclusion (p. 643) that it is the law of New York "that a wrongful breach prior to termination, and not, in itself causing irreparable injury, but causing such injury if the contract were to be terminated, can not defeat the right to terminate expressly granted in the contract".

This seems an extraordinarily antiquated view to be attributed to the New York courts, which have usually been in the forefront of the liberal extension of equitable powers to prevent injustice.

The opinion below admits that it can point to no New York case in any way supporting such a harsh doctrine (and none exist). And the court seems anxious to shun responsibility for such palpable injustice by implying that "considered as an independent question", it might "arrive at a contrary result". It tries to throw the onus on "what the courts of New York would do," but the attempt seems lame in the absence of a single New York authority in point.

The *Cammack* case, *supra,* gives a good indication of how any New York court would act in this case. The court there said (italics supplied): *"of course,* it would be unreasonable *and inequitable"* to permit defendant to exercise an otherwise absolute power to terminate, and continue to sell radiators without paying the agreed compensation.

In other words, the court held that the inequitable conduct of the defendant after giving notice of cancellation voided the notice. Can any one doubt that the same doctrine would apply to inequitable conduct prior to the notice?

As far back as 1890, New York's highest court recognized that an express and absolute power of termination is subject to equitable restrictions. *Lipman* v. *Niagara Fire Ins. Co.*, 121 N. Y. 454, 460, holds that "The privilege reserved by the" (fire insurance) "Company to terminate the policy on notice, cannot be exercised under the circumstances which would make it operate as a fraud on the insured, as in case of notice given pending an approaching conflagration, threatening to destroy the property insured." The *Lipman* case (recently cited with approval in *Friedman* v. *Connecticut General Life Ins. Co.*, 251 A. D. 292, leave to appeal denied, 275 N. Y. 649) is not so strong as ours, for the fire was not set by the insurance company, while here the corresponding circumstances making cancellation inequitable are due to Metals' own misconduct.

Thus clearly New York law does not make an "absolute power to terminate", whether implied or express, a shield for injustice. Cases holding that entirely collateral breaches of contract, not involving irreparable injury, do not bar the exercise of an absolute power to cancel the contract, seem to be wholly inapplicable to the present case, where the breaches are directly connected with the effect of cancellation, and were evidently part of a plan, which cancellation would consummate, to inflict irreparable injury upon DeBothezat by preventing the latter from resuming the fan business, and thus appropriating the entire business to Metals' own use.

What makes the decision of the court below on this point even harder to understand is its concession (p. 644) that under New York law Metals was probably a quasi-fiduciary for DeBothezat in conducting the business. It cites for this proposition *Selwyn & Co.* v. *Waller*, 212 N. Y. 507, 106 N. E. 321. Another case to the same effect is *May*

v. *Hettrick Bros.*, 181 A. D. 3. Nevertheless, the court below ruled that the misconduct of the quasi-fiduciary in wrongfully appropriating to itself alone the business which was the sole object of the trust, was completely beyond the control of a court of equity, once the joint relationship was ended.

The court said that DeBothezat might, before termination, enjoin Metals from suppressing the DeBothezat name and destroying its good-will, and might also get more detailed audits. But this seems rather cold comfort if (as must be assumed to justify striking the defenses) the suppression of the name, and the concealment of operations, had been going on for years, and the contract could be cancelled on six months' notice,—far too short a time to repair the damage.

It seems obvious that the court's proposed remedy would be a mere slap on the wrist, and would not in the least hinder Metals from accomplishing its unlawful end,—the appropriation of the whole fan business to its own use without the payment specified therefor in the contract. Assuming (as we must) that the court were convinced that Metals' scheme would prevent DeBothezat from resuming business at all, due to the wrongful suppression of its name over a long period of years, which could not be cured by a few months' enforced use before termination, the opinion below holds that New York law is powerless to prevent the theft of the joint business by the faithless fiduciary. And more than this, DeBothezat has been here stayed from pressing its counterclaims, so that as a practical matter even the pitifully inadequate relief suggested below as possible, has been wholly denied. For this extraordinary tenderness for fraud—on the alleged ground of public policy—the court cites *three Federal patent cases.*

The law of New York is in no way so impotent in dealing with inequitable conduct as has been hitherto held herein. One example of the way in which somewhat similar wrongdoing was dealt with is found in *Russell H. & I. M. Co.*

v. *Utica D. F. & T. Co.*, 195 N. Y. 54, 87 N. E. 788. This case was (curiously enough) relied upon in the District Court's opinion striking the defenses, but was not mentioned in the affirming opinion. There, due to evidence of defendant's wrongful acts committed after the pleadings were filed, the Court of Appeals affirmed a decree enjoining defendant "from further exercise of any of the rights in the *business, trade and good will* of the Russell staple puller," etc. An analogous decree in this case might enjoin Metals upon termination "from further exercise of any of the rights in the business, trade, good-will, and trademarks of its DeBothezat Fans Division." Such a decree (though less drastic than one preventing termination altogether, or prohibiting Metals from the fan field entirely) would effectively prevent Metals from carrying on the *DeBothezat fan business* (minus the name only) with fans which are described by Metals itself as "based on Dr. DeBothezat's original concepts" and "designs" (p. 408). It would not prevent Metals from starting a new fan business of its own, with entirely new designs and customers. Just which form of decree would adequately circumvent Metals' unlawful scheme on this point alone (quite apart from Points I and II, *supra*) would be for the court to decide, after weighing the evidence of Metals' misconduct. But it would certainly go further than the decree approved below, which merely adopted the innocuous concession in Metals' own complaint (p. 7) that it be restrained from "infringing upon valid patents owned" by DeBothezat,—a mild restraint to which every person in the United States is equally subject!

The opinion of Chief Judge Cardozo, writing for the unamimous court in *Meinhard* v. *Salmon*, 249 N. Y. 458, stressed the accountability of the manager of a joint venture to his inactive associate, with respect to an option which became available shortly before the joint venture terminated. The business opportunity which Metals is accused of misusing here, is the entire existing DeBothezat fan business.

The doctrine that the managing partner of a joint business can over a period of years unlawfully suppress the partnership name and substitute another, then dissolve the partnership and continue to run the stolen business as his own under the other name, without being subject to equitable restraint, has only to be stated to be denied. Yet that seems the clear implication of the decisions below, which in this respect again conflict with New York law.

The holdings below would establish (in the name of public policy!) a simple pattern of wrongdoing whereby large corporations like Metals could steal small businesses like DeBothezat's, with the acquiescence of the court, and even with their active help, as here, in enjoining the defrauded obligee from seeking equitable relief until the theft is securely consummated.

We respectfully submit that such a gravely unjust principle (or lack of principle), fraught with such serious anti-social consequences, is quite at variance with the settled law of New York State, and should not be approved even tacitly by the Supreme Court of the United States.

CONCLUSION

The petition for a writ of certiorari should be granted.

New York, April 1950.

Respectfully submitted,

McLaughlin, Stickles & Hayden,
Attorneys for Petitioner,
36 West 44th Street,
New York 18, N. Y.

Samuel Williston,
Chester B. McLaughlin,
Watson Washburn,
Of Counsel.